ontario financing authority

2002 Annual Report

Ontario

Ontario Financing Authority

103-01410/

Profile

On behalf of the Province of Ontario, its Crown corporations and other public bodies, the Ontario Financing Authority:

- executes all borrowing, investment and financial risk management activities;
- manages the Provincial debt;
- advises on financial policies and projects;
- provides financial and cash management services;
- provides financial services and advice to the Ontario Electricity Financial Corporation; and
- operates the Province of Ontario Savings Office.

As an agency of the Province, the Ontario Financing Authority reports to the Minister of Finance who is accountable to Cabinet for the activities of the Ontario Financing Authority.

Highlights in 2001-02

The Province's long-term public borrowing program of $12.3 billion was completed in a sound and cost-effective manner. Through the timing of debt issues and related hedging, the cost of borrowing for the Province and Ontario Electricity Financial Corporation during the fiscal year is estimated at $75 million less than the benchmark, on a present value basis.

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The seventh annual Ontario Savings Bonds campaign raised $4.2 billion, the biggest provincial savings bond campaign in Canadian history.

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Three bond auctions raising $750 million saved the Province approximately $1.5 million in commission costs. Aided by a more efficient documentation process, over 35 Medium-Term Notes (MTN) were issued for $2.2 billion, a significant increase from the previous year when only seven MTNs were issued.

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The Ontario Financing Authority coordinated the Government's efforts to obtain credit rating upgrades. The Dominion Bond Rating Service (DBRS) raised its issuer credit rating on the Province of Ontario to double "A" from double "A" (Low).

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The Ontario Financing Authority provided financing advice to school boards. One school board saved approximately $2.5 million based on the advice.

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The realignment of several banking services between banking service providers is expected to reduce banking fees by about $450,000 annually.

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Statement from the Chair

It is with pleasure that I present the 2002 Annual Report of the Ontario Financing Authority. This report outlines the Ontario Financing Authority's objectives and responsibilities, operational highlights and financial results for the year April 1, 2001 to March 31, 2002 and includes priorities for the next year.

The downturn in the U.S. economy and the disruptions to trade following the events of September 2001 caused Ontario's economy to slow. Ontario's economy grew by only 1.0 per cent in 2001, after a 5.3 per cent advance in the previous year.

Tax cuts and other policies implemented by the Ontario Government cushioned the negative impact of the U.S. downturn and the subsequent fall in demand for Ontario products, particularly autos and telecommunication equipment. These policies are now helping the economy resume strong growth. Ontario's economy is forecast to grow by 3.1 per cent in 2002. Reports on job creation, consumer and business confidence, consumer spending and housing markets all point to renewed vigorous growth.

Despite the economic slowdown in 2001, Ontario made a contribution of $127 million to debt reduction during the 2001-02 fiscal year. Through combined reductions of $1.0 billion in 1999-2000 and $3.1 billion in 2000-01, Net Provincial Debt has been reduced by $4.2 billion over the past three years, an amount representing almost 85 per cent of the government's $5 billion debt reduction commitment for the current term of office.

Finally, I'd like to thank Gadi Mayman for his hard work and dedication as interim Chief Executive Officer, and look forward to working with Michael Gourley who took over as Chief Executive Officer effective July 1, 2002.

Bob Christie
Chair
Ontario Financing Authority

Statement from the Chief Executive Officer

I am pleased to have been appointed in July 2002 as Vice-Chair and Chief Executive Officer of the Ontario Financing Authority.

In this year of unexpected events, the Ontario Financing Authority was able to achieve its primary goal of borrowing $12.3 billion on competitive terms and conditions in long-term public markets.

For the second fiscal year in a row, the Ontario Financing Authority was successful in coordinating the Government's efforts to obtain an upgrade from a credit rating agency. The Dominion Bond Rating Service (DBRS) raised its credit rating on the Province of Ontario to double "A" from double "A" (Low), following post-budget consultations.

The bond auction program initiated last year continued to provide savings to the Province with a further three auctions taking place. The three bond auctions raised $750 million and resulted in an estimated savings of $1.5 million in commission costs.

Financing advice was provided to a number of entities in the broader public sector including school boards both individually and through the Ontario School Boards Financing Corporation. In one case, a school board saved as much as $2.5 million due to the Ontario Financing Authority's input.

We have a number of challenging assignments in the next fiscal year. These include the implementation of the Integrated Financial Information System (IFIS), which is an enterprise-wide integrated financial management system for the Ontario Government, preparing the Ontario Electricity Financial Corporation (OEFC) for competition in the electricity market, and refinancing debt maturities of $11.7 billion.

We at the Ontario Financing Authority are committed to the successful completion of our 2002-03 objectives, providing Ontario taxpayers with continued cost-effective and prudent borrowing and debt management.

Michael L. Gourley
Vice-Chair and Chief Executive Officer
Ontario Financing Authority

Objectives and Responsibilities

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The Board of Directors

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Human Resources Objectives

Objectives and Responsibilities

The Ontario Financing Authority (OFA) was established by the *Capital Investment Plan Act, 1993*. The OFA performs the following responsibilities for the Province of Ontario, its Crown corporations and other public bodies:

- Executes Borrowing, Investment and Financial Risk Management Activities

The primary goal of the Ontario Financing Authority is to meet the Province's financial requirements in a sound and cost-effective manner.

- Manages the Debt of the Province

The OFA manages the Province's debt and contributes to the government's debt reduction efforts. The key principles guiding the management of the debt and associated risks are soundness, efficiency, a smooth debt maturity profile and safeguarding Ontario's credit rating.

- Advises on Financial Policies and Projects

The OFA provides financial policy advice to the Ontario Government on a wide range of corporate finance issues. Examples include electricity industry restructuring, public-private partnerships, sale of Government assets and alternative financing proposals.

- Provides Financial and Cash Management Services

The OFA provides cash management and banking-related services and advice to the Province. In addition, the OFA undertakes the accounting and trade settlement for the Province's liquid reserve portfolio, debt portfolio and related hedging transactions.

- Provides Financial Services and Advice to the Ontario Electricity Financial Corporation

The OFA provides financial services and advice to the Ontario Electricity Financial Corporation (OEFC). The OEFC is the agency responsible for servicing and retiring the former Ontario Hydro's provincially guaranteed debt and certain other liabilities of the former Ontario Hydro.

- Operates the Province of Ontario Savings Office

The OFA will continue to operate the Province of Ontario Savings Office (POSO), until its privatization is completed. Currently, POSO has 23 branches, four agencies and one office.

The Board of Directors

Appointed by the Lieutenant Governor in Council, the Board of Directors supervises the business of the Ontario Financing Authority through a number of processes. For example, it approves the OFA's business plan and receives regular reports regarding financing activities. The business plan sets out the OFA's major objectives and the strategies for achieving them. It is revised annually, and approved by the Minister of Finance. The Board also approves the Province's annual financing and debt management plan and key policies applied by the OFA in capital market transactions and management of the Province's debt and investment portfolios. The Board's Audit Committee reviews the financial statements of the OFA, including the Provincial Auditor's report, for recommendation to the Board; oversees the internal audit process; and receives the advice of internal auditors and the Provincial Auditor regarding the adequacy of internal controls.

The Board of Directors meets at least quarterly. Throughout 2001-02, the Board of Directors was composed of the Deputy Minister of Finance, the Chief Executive Officer of the OFA, and four members from the private sector. The directors' diverse backgrounds contribute to the effective supervision of the OFA.

The following individuals were members of the Ontario Financing Authority's Board of Directors in 2001-02:

Dr. Bob Christie, Chair of the Ontario Financing Authority Board of Directors and Deputy Minister of Finance. (Appointed to the OFA Board of Directors in August 2000. Appointment expires when successor appointed.)

Michael L. Gourley was appointed Vice-Chair and Chief Executive Officer of the Ontario Financing Authority, effective July 1, 2002. (Appointed to the OFA Board of Directors from July 2002 to June 2005.)

Gadi Mayman, Vice-Chair and Chief Executive Officer, Ontario Financing Authority. (Interim appointment from August 2000 to June 30, 2002).

John Callendo, Managing Director, Cornerstone Partners Ltd. (Appointed to the OFA Board of Directors from July 2000 to July 2003.)

Winnie Wong, Partner, Wong Po Partners, Chartered Accountants LLP. (Appointed to the OFA Board of Directors from July 2000 to July 2003.)

Frank Potter, Chairman of Emerging Markets Advisors Inc., Toronto. (Appointed to the OFA Board of Directors from May 2002 to May 2005.)

Tye W. Burt, President of Cartesian Capital Corporation, a venture capital and private equity firm. (Appointed to the OFA Board of Directors from June 2000 to June 2003.)

Human Resources Objectives

As with all organizations, the Ontario Financing Authority faces a changing workplace. Changing workplaces require organizations to rethink roles, structures and ways of delivering services. The OFA is committed to meet these challenges and provide a high level of service to its stakeholders.

In this regard, several human resource strategies initiated in 2000-01 continued to be implemented or enhanced in 2001-02. Staff participated in secondments, held memberships on committees, task forces and projects, and were given opportunities to improve technical, communication, management and knowledge-based skills.

The OFA took part in Ontario Public Service (OPS) wide initiatives such as the Internship Program and workfare initiatives, which are aimed at providing training and work experience. As well, a number of divisions hired students through various university cooperative work placement programs. Through annual performance reviews and training programs, opportunities were identified and staff were encouraged to work towards obtaining performance objectives either through formal courses or on-the-job training.

To this end, a number of staff pursued educational courses such as the Chartered Financial Analyst (CFA), and various accounting programs such as the Certified Management Accountant (CMA) and the Certified General Accountant (CGA) designations. Staff were also encouraged to attend conferences, seminars or presentations to keep abreast of advances in finance, accounting and technology. Working with human resource consultants of the Ministry of Finance, the OFA took steps to improve succession planning and retain staff for longer periods. The objective of these human resource initiatives is to improve the attractiveness of the OFA as a place of employment, reduce turnover, and therefore increase efficiency, which ultimately benefits stakeholders.

Management's Discussion and Analysis

This section of the Annual Report provides management's discussion and analysis of the business environment, accomplishments in 2001-02 and objectives for 2002-03.

The Business Environment

Capital Markets Division

Risk Control Division

Corporate Finance Division

Capital Markets Treasury Division

Province of Ontario Savings Office

The Business Environment 2001

Financial Markets in Review

Financial markets experienced uncertainty throughout 2001-02. A series of cuts in the trend-setting U.S. Federal Funds rate began at the start of 2001, when signs emerged that the American economy was slowing down. The Federal Reserve cut rates 11 times for a total of 4.75 per in 2001, ending at 1.75 per cent, a 40-year low. The Bank of Canada also responded to the economic slowdown by cutting interest rates nine times in 2001, with its target for the overnight rate falling by 3.50 per cent to 2.25 per cent at year-end. On January 15, 2002, the Bank of Canada lowered its target for the overnight rate by a further 25 basis points to 2.00 per cent. The recent strength of the economy prompted the Bank of Canada to raise interest rates a quarter of a percentage point twice, once in mid-April and again in early June, for the purpose of reducing the amount of monetary stimulus in the economy.

Despite the dramatic fall in short-term rates, yields on 10-year U.S. Treasury, Canada and Ontario bonds remained relatively unchanged throughout 2001. Canadian 10-year bond yields resumed their historic pattern, trading above their U.S. counterparts during the year due in part to weakness in the Canadian dollar and less aggressive rate cutting by the Bank of Canada.

The Canadian dollar weakened throughout 2001 and touched all-time lows in January 2002, but strengthened towards the end of fiscal year 2001-02, as evidence accumulated that the slowdown in Canada in 2001 was less pronounced than in the United States, and as the recovery in 2002 has been both quicker and stronger in Canada than in the United States. Further support to the Canadian dollar was provided by the Bank of Canada, as it raised its overnight rate twice by 25 basis points in mid-April 2002 and early June, increasing the interest rate differential versus the United States.

Economic Review

As with most provinces, Ontario experienced a sharp economic slowdown in 2001, with real GDP rising 1.0 per cent, after posting a 5.3 per cent gain in 2000. Final domestic demand growth slowed, the result of weaker consumer spending and a drop in business investment. Exports also fell, while business undertook a large $2.9 billion inventory depletion.

On the income side, nominal GDP growth slowed from 5.9 per cent to 2.4 per cent in 2001. Corporate profits were down for the year, after eight consecutive annual gains.

On the industry side, output in the computer and electronics industry tumbled. Manufacturing output also fell, especially in the auto sector. The events of September 11, 2001 also curtailed the growth in other industries, particularly the transportation sector.

Prices, measured by the GDP price deflator, rose 1.4 per cent in 2001, up from the 0.6 per cent advance in 2000.

Technology

Following September 11, 2001, many organizations began to seriously reassess their security initiatives to determine areas of improvement. Security has always been important to the OFA and network security was the top priority in 2001.

Some of the OFA's key security initiatives included enhancing security monitoring systems, implementing effective perimeter-type defences and keeping skilled resources. Obtaining security certification was another key initiative. TruSecure, a firm that specializes in security assessments, was hired to evaluate the security of the OFA's network perimeter and internal technology infrastructure. The OFA subsequently obtained the firm's certification that its security controls, policies and procedures met very stringent requirements.

An influx of computer viruses also occurred in 2001. Viruses have become more sophisticated even as anti-virus defences continue to advance. The OFA has effectively limited its exposure to these computer threats by utilizing various monitoring and filtering tools as well as ensuring security patches are up todate.

In an effort to expand the use of technology as a means of efficiently communicating with bond investors, the OFA sponsored the Province's first webcast on February 27, 2002, presenting the Province's Third Quarter Finances. The OFA received positive feedback from the financial community on the initiative, and as a result, future webcasts are planned for fiscal 2002-03.

In 2002-03, the OFA will continue to monitor the information technology and financial industries to ensure that its systems are capable of maintaining their existing high level of service in a cost-effective and secure manner.

Capital Markets Division

Responsibilities

- Execute borrowing program and debt management activities.
- Manage legal requirements and securities commission filings.
- Manage relations with investors and the investment community.

2001-02 Accomplishments

The OFA's primary objective is to ensure that both the Province's and OEFC's financing and liquidity needs are met cost-effectively, minimizing interest costs within approved risk policies and exposure limits. In 2001-02, borrowing of $12.3 billion was completed in the long-term public markets, mainly to fund maturing debt, adjustments for non-cash items included in the surplus and early bond redemptions. Of the $12.3 billion in long-term public borrowing, $10.3 billion was borrowed from the Canadian dollar market and $2.0 billion from the U.S. dollar market.

The OFA also completed $1.8 billion of long-term public borrowing on behalf of the OEFC. This borrowing was done in the Canadian dollar market. The remaining borrowing requirement of $1.6 billion was funded using short-term debt, since it was more cost-effective.

The 2001 Ontario Savings Bond (OSB) campaign, the seventh issue of OSBs, raised $4.2 billion, a Canadian provincial record.

Timing of Debt Issues

Through the timing of debt issues and related hedging, the cost of borrowing for the Province and OEFC during fiscal 2001-02 is estimated at $75 million less than the benchmark, on a present value basis. This performance measure compares the actual cost of borrowing against a benchmark of hypothetical domestic borrowing of the same term spread out evenly over the fiscal year based on projected borrowing requirements.

Reducing the Cost of Borrowing

Building on the successes of last year's bond auctions, the Province completed three bond auctions this fiscal year raising $750 million and saving the Province approximately $1.5 million in commission costs. The results were posted on the OFA's website, www.ofina.on.ca.

As of January 2002, Ontario Treasury Bills became eligible for deposit in the Canadian Depository Services Debt Clearing System. This new process eliminates the expense of printing and safeguarding physical certificates, which increases the efficiency of treasury bill issuance, as it reduces the administration requirements and eliminates the possibility of fraud and forgery inherent in the issuance and trading of physical securities.

Capital Markets Division

Financing Sources

The 2001-02 borrowing program was again heavily reliant on the Canadian dollar market. Over 80 per cent of $12.3 billion in long-term borrowing was completed in Canadian dollars. Canadian dollar market borrowing included $4.2 billion from the seventh issue of Ontario Savings Bonds (OSB) and $0.8 billion from seven Euro-Canadian dollar issues.

Another significant source of Canadian dollar market borrowing was accomplished through the Province's Medium-Term Notes (MTN) program. The medium-term note market was active in the fiscal year, particularly with respect to retail borrowing opportunities. During the fiscal year, over 35 MTNs were issued for $2.2 billion, a significant increase compared to the previous year, when only seven MTNs were issued. A new domestic MTN documentation process reduced paperwork and legal costs, enabling cost-effective, smaller deal sizes. These efficiencies were in part responsible for the increased level of domestic MTN market activity.

There were several opportunities for the Province to issue U.S. dollar debt and hedge the proceeds back into Canadian dollars at costs below the Province's domestic borrowing costs. The Province reopened U.S. dollar global issues on four occasions and issued a U.S. dollar Yankee bond. This was the first U.S. dollar Yankee bond that Ontario had issued in over 10 years. The Yankee format was selected for its lower legal, documentation and stock exchange listing fees relative to a U.S. dollar global issue and was targeted to a small number of U.S. institutional investors.

The Province chose not to utilize its share of Canada Pension Plan (CPP) funds for financing, as this source of funding was more expensive than alternative funding sources.

Finally, the Province issued over $700 million of 40-year bonds at all-in costs substantially below 30-year issues.

Debt Management Activities

In order to take advantage of market opportunities and save money, the OFA repurchased several Ontario debt issues and replaced them with more cost-effective issuance.

The OFA uses financial options and swaps to manage the Province's exposure to fluctuations in interest rates and foreign currency exchange rates. Risk exposures are monitored daily and audited annually. The cost-effectiveness of borrowing, debt management and investment activities are measured daily against pre-established benchmarks.

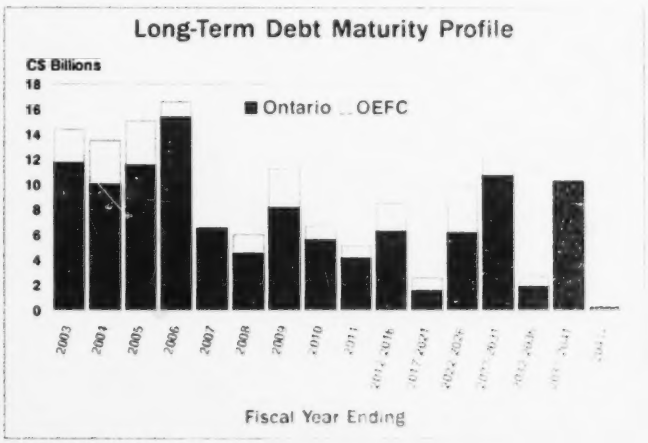
As of March 31, 2002, the Province's total swap portfolio had a notional value of $72.2 billion, which consisted of $30.0 billion in cross-currency swaps and $42.2 billion in interest rate swaps.

To mitigate the financial risks inherent in a large and diversified debt portfolio, it is important to maintain prudent risk management policies and practices. The table on page 15 represents the limits and strategies the OFA employs to ensure that market, credit and liquidity risks are managed in a sound and cost-effective manner.

Policy		Status
Foreign Exchange Risk	The Province's exposure to unhedged foreign currency exposure is limited to 5 per cent of outstanding debt.	Net foreign exchange exposure was 1.5 per cent of outstanding debt as of March 31, 2002. During the fiscal year, foreign exchange exposure was within approved limits.
Interest Rate Resetting Risk	The Province's exposure to interest rate resetting risk is the combination of net floating rate exposure (i.e., gross floating rate exposure less liquid reserves) and all fixed rate debt maturing within the next 12-month period. The Province is limited to having a maximum interest rate reset exposure of 25 per cent of outstanding debt.	Interest rate resetting exposure was 12.5 per cent of outstanding debt as of March 31, 2002. During the fiscal year, floating interest rate exposure was within approved limits.
Refinancing Risk	Term selection for new borrowing is aimed at achieving a smooth maturity schedule to diversify the interest resetting risk of refinancing debt maturities.	During 2001-02, maturities amounted to $9.5 billion. In 2002-03, maturities are estimated at $11.7 billion.
Credit Risk	Ontario typically enters into new transactions with counterparties rated "AA minus" or higher.	At year-end, 80 per cent of the swaps outstanding were with financial institutions with credit rating "AA minus" or higher.
Liquidity Risk	Liquidity risk is controlled through the management of liquid reserve levels, short-term borrowing programs and prearranged lines of credit.	The average level of liquid reserves was $5.0 billion in 2001-02. The Province's Treasury Bill and U.S. Commercial Paper programs have authorized limits of $9.0 billion ($6.0 billion for the Province and $3.0 billion for the OEFC) and $2.5 billion, respectively.

Priorities for 2002-03

The Province's total long-term public borrowing for 2002-03 is projected at $12.7 billion, of which $11.7 billion is to refinance maturing debt. $1.2 billion is a provision for early redemptions of debt. $2.9 billion is related to adjustments for non-cash items included in the surplus, and $1.4 billion is related to acquisitions of tangible capital assets. These requirements are partially offset by a decrease in cash of $3.0 billion and the amortization of tangible capital assets of $0.7 billion. The high level of maturing debt over the next four years coupled with a rising interest rate environment will require significant attention to be paid to prudent debt management practices.



The majority of borrowing will likely be completed in the domestic market. An additional source of domestic borrowing may be the Canada Pension Plan (CPP). The actual amount borrowed from the CPP will depend on whether it is cost-effective relative to other financing alternatives. In addition, an eighth issue of Ontario Savings Bonds will be included in the 2002-03 financing program. The size of the campaign will depend on market conditions.

International capital markets will be monitored and foreign markets will be accessed when total borrowing costs are lower than those in the Canadian domestic market.

The Province plans to look at the feasibility of offering Ontario Savings Bonds using the Internet. The OFA will continue to build on the successes of its bond auctions and domestic MTN program.

The OFA also plans to borrow on behalf of the Ontario Electricity Financial Corporation (OEFC). OEFC's debt maturities for 2002-03 are $2.7 billion.

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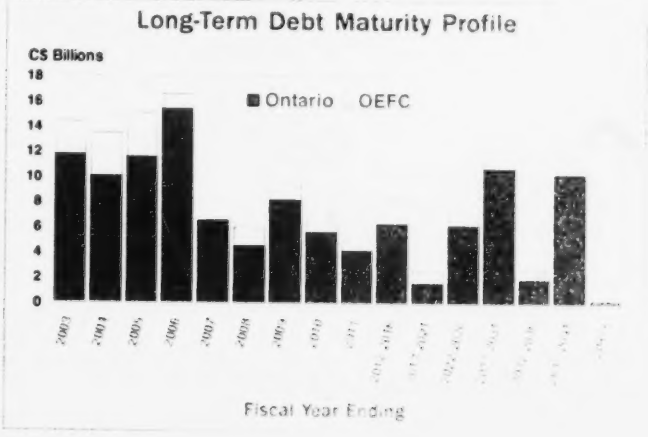

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Risk Control Division

Responsibilities

- Monitor and measure financial risks and performance associated with borrowing, debt management and investment of liquid reserves.
- Ensure risk management policies reflect prevailing market conditions, address counterparty exposures and monitor compliance.
- Develop risk management policies and monitor compliance to new business exposures.
- Forecast and analyze Public Debt Interest for the Provincial budget and quarterly fiscal updates.
- Assess counterparty credit risk and manage rating agency relations.
- Provide systems development and information technology support.

2001-02 Accomplishments

The division obtained Board approval of amendments to the OFA and OEFC Policies on Credit and Related Legal Risks clarifying the criteria for establishing and revising credit limits for counterparties and addressing the event of counterparty mergers. These amendments are in line with industry best practices.

The division also obtained OEFC Board approval of the Policy Framework for Risk Management of Non-Utility Generation Contract (NUGs) Power Sales, which will be used as a basis for developing OEFC electricity-related risk management policies, and procedures for the prudent assessment and management of associated market and counterparty credit risks. In association with the underlying policy framework, the division has undertaken an OFA-wide initiative to identify and develop essential management information and reporting systems in support of portfolio management, settlements and risk assessment.

In consultation with legal counsel, Ministry of Finance Internal Audit, and other jurisdictions, the division amended the OFA Policy on Trading Restrictions pertaining to specific staff disclosure requirements and establishing the role of "Compliance Officer" (the CEO or a person designated by the CEO) to administer these requirements, imposing temporary trading restrictions as necessary. These revisions are in accordance with industry best practices and have been fully implemented.

A framework for stress testing and scenario analysis for evaluating the Financing and Debt Management Programs was implemented beginning in the 2001-02 fiscal year.

The use of risk budgeting and risk-adjusted performance evaluation to measure the effectiveness of the Debt Management Program, implemented on a trial basis in 1999-2000, were continued in the 2001-02 fiscal year. The suitability of this approach for other programs is being assessed as part of an ongoing study on performance measurement.

As part of the Integrated Treasury System (ITS) project, the division is consolidating all counterparty and associated market and credit exposure measurement assessment, monitoring, and reporting. This will eliminate data duplication and improve data quality, compliance monitoring and reporting. All credit exposure reports will be based on ITS data. This initiative is presently in the testing phase and is expected to be completed by mid-2002.

The division coordinated the annual post-budget meetings with credit rating agencies after the release of the 2001 Budget. Following post-budget consultations, Dominion Bond Rating Service (DBRS) raised the Province's issuer credit rating to double "A" from double "A" (Low). This was the third consecutive upgrade on the Province's credit rating by DBRS. The AA rating by Standard & Poor's, and the Aa3(P) rating by Moody's Investors Service were confirmed following the agencies' respective reviews.

Public Debt Interest (PDI) forecasting models and procedures were reviewed by Internal Audit and their recommendations are being implemented. PDI reforecasting and variance analyses are now prepared on a monthly basis with corresponding briefing notes to the CEO.

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Public Debt Interest (PDI) forecasting models and procedures were reviewed by Internal Audit and their recommendations are being implemented. PDI reforecasting and variance analyses are now prepared on a monthly basis with corresponding briefing notes to the CEO.

Procedures conforming to industry best practices for assessing model risk have been adopted and work on testing models is underway. Several key mark-to-market pricing models have been reviewed. Internal Audit has been asked to review this initiative and to make recommendations.

To mitigate operational risk, the division tabled before the Borrowing Strategy Committee and the respective Boards of Directors of both the OFA and OEFC, the ITS Control Principles for Electronic Trade Authorization Processes. These initiatives, in conjunction with the Mid-Office Data Base (MODB) Compare Utility (designed to ensure the MODB captures all transactions in the systems of record), were endorsed by Ministry of Finance's Internal Audit as appropriate measures.

The division has undertaken other projects (in conjunction with other jurisdictions and independently) to keep abreast of advances in the fields of risk control and portfolio benchmarking.

The Information Technology (IT) systems and technology infrastructure support all of the OFA's core business objectives. During 2001-02, the availability and performance of IT systems and technology platform were maintained at a high level. A better than 99.9% availability of the network, production and end-user servers was achieved. Redundant LAN switches and adaptor fault tolerance for all critical servers, as well as increases in network bandwidth were implemented to ensure real-time availability. Windows NT and Novell servers were migrated to Windows 2000 servers. Storage Area Network-based technology was introduced to support the clustering of file and print services. As well, database servers were modified to support clustering using quadruple processing technology.

Application systems support primary businesses such as cash management, investing, borrowing and risk management. The ITS, which will support the OFA's core treasury operations, was completed during 2001-02. The first phase of the Treasury Accounting System (TAS) was developed and implemented. ITS provides comprehensive accounting functionality related to debt, investments and PDI for the Province, OFA and OEFC. It also meets various reporting requirements, including year end accrual reports. TAS will integrate and be compatible with both ITS and the new government-wide Integrated Financial Information Systems (IFIS), which are currently being implemented.

A wide range of security systems and procedures are in place to protect the OFA's technology infrastructure. During 2001-02, protective measures against threats from the Internet were significantly increased by adding intrusion detection systems and enhancing virus scanning and firewall systems. A year-long series of comprehensive evaluations and tests of the OFA's technology infrastructure security and risk reduction procedures were completed by TruSecure, a worldwide leader in security assurance solutions, and the OFA has received TruSecure's security certification. This industry-recognized certification provides assurance, including a guarantee by TruSecure, that the OFA is protected against cyber threats and demonstrates that the OFA has made security a priority, is employing top quality security systems and practices, and is maintaining a proactive and comprehensive information security program.

Priorities for 2002-03

During 2002-03, the division will continue to enhance or update its financial risk assessment capabilities, portfolio analytics, financial risk measures and risk management policies for OFA, OEFC and NUGs. This will include conducting strategic studies as required, e.g., NUG-related risk measurement and portfolio analysis and target debt portfolio and performance benchmarking for the Province.

Work will continue on core functions, such as risk measurement and performance reporting, monitoring of compliance of program positions, monitoring model risk, projecting the PDI budget and analyzing variances, enhancing market and credit risk monitoring, and reviewing and improving performance evaluation models. The priority with respect to these key deliverables is to improve operating efficiencies while enhancing the analytic tools and management reporting capabilities of the division.

Regular communications with credit rating agencies will continue to ensure that the Province's ratings are based on current and timely information.

Finally, the division will continue to keep the OFA's IT systems and technology infrastructure capacity and capability in step with the OFA's growing business needs. Application systems will continue to be enhanced and become more integrated with other systems, both internally (with ITS as the foundation) and externally (to systems such as IFIS). Internet and security systems will remain a high priority issue. The OFA will ensure that it maintains its solid security posture and will keep pace with the changing and emerging Internet and security technologies.

Corporate Finance Division

Responsibilities

- Advise on financial policy issues.
- Advise on financing approaches for the broader public sector.
- Advise on the financial implications of potential privatizations.
- Develop financial options for Ontario agencies and Crown corporations.

2001-02 Accomplishments

The Corporate Finance division accomplished a significant number of objectives on behalf of the OFA in 2001-02. The division was significantly involved in providing advice on many aspects of electricity restructuring. This included acting on behalf of OEFC to advance negotiations to revise the non-utility generation contracts to facilitate their integration into the open market.

Corporate Finance continued to be active in assisting Ontario SuperBuild Corporation on a number of projects including the extension of Highway 407 to Highway 35/115, the development of the Durham Courthouse through a public-private partnership and the privatization of the Province of Ontario Savings Office, as well as numerous other projects.

The division worked jointly with ministries and agencies and their stakeholders to provide financing advice in a number of areas. For instance, the division worked with the Ministry of Health and Long-Term Care and a group of stakeholders to coordinate the retention of an external financial advisor to determine whether pooled financing could lower financing costs in the sector and speed the delivery of long-term care facilities. Assistance was provided to the Ontario Lottery and Gaming Corporation in developing an appropriate financing model for the Niagara Casino. Also, a new mechanism to fund student loans under the Ontario Student Assistance Program was developed and implemented.

Financing advice was provided to a number of entities in the broader public sector including school boards both individually and through the Ontario School Boards Financing Corporation. In one case, a school board saved as much as $2.5 million due to the division's input. Advice was also provided to a group of municipally owned electricity distribution companies that have decided to issue debt on a pooled basis.

Finally, the division became more active in the leasing activities of ministries as a result of a number of high profile cases where leasing activities in the broader public sector turned out to be less favourable than originally anticipated.

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Corporate Finance Division

Priorities for 2002-03

The division will continue to assist the Province in the restructuring of the electricity industry. This will include assisting the Ontario SuperBuild Corporation, working with the Office of Electricity Restructuring and providing services to OEFC.

Services to OEFC will focus on the continued development and finalization of internal risk management systems to manage the NUG contracts and the trading of the electricity that OEFC will purchase from the NUGs. Other services will include the ongoing management of OEFC's debt and other liabilities, and re-evaluating the feasibility of auctioning the NUG contracts after the electricity market opens in May 2002.

The division will be working with the ministries of Finance and Municipal Affairs and Housing to implement the Throne Speech initiative to allow municipalities to issue tax-free opportunity bonds.

Assistance will be provided to ministries and agencies on a number of projects:

- the Ministry of Enterprise, Opportunity and Innovation on the International Thermonuclear Experimental Reactor (ITER) Canada project;
- the Ministry of Northern Development and Mines on the restructuring of the Ontario Northland Transportation Commission;
- the Ontario Lottery and Gaming Corporation on the financing of the Niagara Casino;
- the Ministry of Municipal Affairs and Housing on the development of borrowing, leasing and investment regulations; and
- the Ministry of Culture on the financing of the Royal Ontario Museum Renaissance Redevelopment Project.

The division will develop a formal policy on providing financial advice and assistance to members of the broader public sector where it serves to advance provincial policy interests and reduce costs to taxpayers. In the interim, the division will continue to provide advice and assistance on a case-by-case basis. This will include activities in the long-term care and local electricity distribution sectors.

The division will continue to assist Ontario SuperBuild Corporation in the review of other projects such as the extension of Highway 407, courthouses and the Province of Ontario Savings Office as well as any other new projects.

To ensure that taxpayers are receiving good value, a review of leasing activities in various ministries has been initiated and will be finalized in 2002-03.

Capital Markets Treasury Division

Responsibilities

- Lead government-wide initiatives aimed at centralizing the Province's cash management and financial services activities.
- Provide cash management services for the Province.
- Settle debt, securities and derivatives transactions.
- Provide banking advice regarding Consolidated Revenue Fund revenues and disbursements.
- Manage banking and fiscal agency relations.
- Generate accounting, financial and management reporting.
- Advise on accounting issues and their implications.

2001-02 Accomplishments

A number of initiatives were implemented to improve the timing of the Province's cash flows, enhance financial services to ministries and Crown agencies, and strengthen internal operations and controls.

Cash Management

To promote cash management awareness and business-like cash management practices and the provision of timely and accurate cash management information, the division participated in the Integrated Financial Information System (IFIS) through interministry taskforces and working groups. The objective of the IFIS project is to develop a single enterprise-wide integrated financial information system for the Ontario Government. The full-time secondment of division staff to the IFIS project team provided assurance that cash requirements and cash control over payments would be an integral part of IFIS, thereby enhancing cash management in the Province.

Internally, cash management moved forward on a number of fronts through the enhancement of cash systems to provide better forecasts and more detailed information to the Capital Markets Division to optimize both the investment of cash resources as well as meet cash shortfalls. Cash management also continued with enhancements to the OEFC system including better forecasting and the seamless incorporation of relevant OEFC activities within the Province's cashflows. These improvements to management information contributed to better decision-making on debt management.

Banking Services

Throughout 2001-02, the division continued to work with the Ministry of Finance, Management Board Secretariat E-Government Branch, Ministry of Consumer and Business Services Integrated Service Delivery Division and other line ministries to design and implement cost-effective revenue collection and payment channels. In particular, several ministries introduced Internet web sites whereby the public can acquire and pay for products and services using credit cards. Also, an e-file service was introduced by the Ministry of Finance permitting the public to submit and settle retail sales taxes.

The Province's banking and cash management services were successfully tendered for a further five-year term commencing February 1, 2002. Realignment of several banking services between providers occurred to ensure the lowest costs are incurred. This is expected to reduce annual banking fees by about $450,000.

The division completed implementation of credit card (Visa and MasterCard), debit card and AMEX services for a further five-year term. These contracts were negotiated in 2000-01.

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Accounting and Settlements

Enhancements to the accounting, settlement, payment and forecasting services of OEFC continued in 2000-01. Since 1999-2000, when the OFA assumed the management of OEFC debt, staff and support systems have been organized and procedures improved to accommodate complexity, and workload, including activities pertaining to non-utility generation contracts. Planning has been initiated to prepare for the electricity market opening in May 2002.

Testing of the new Integrated Treasury System (ITS) started in the fall of 2001 with implementation completed in March 2002. The new system will improve processes, accuracy, timeliness and efficiency of settlements, recording and payments. Ongoing review of the industry best practices regarding settlements and fiscal agency functions has continued. Further enhancements to settlement processes to meet industry practices will also be facilitated by the ITS.

With respect to accounting, foreign exchange translation research was provided for review by the Public Sector Accounting Board (PSAB) of the Canadian Institute of Chartered Accountants (CICA). Further research on accounting for financial instruments will be continued. The division continued to work with the IFIS project to ensure that the financial and management reporting needs of the Province and the OFA are met.

Priorities for 2002-03

Cash Management

The division will focus on areas of cash volatility. Through working with the Revenue Operations and Client Services Branch and Fiscal and Financial Policy Division of the Ministry of Finance, the Shared Services Bureau, and other ministries and central agencies, the division will implement systems and process-based solutions to reduce volatility and optimize cash management for the Province.

The division will continue with its involvement in the IFIS project to ensure that the OFA's cash management needs are satisfactorily met and the new system contributes to better forecasts of cash information, thereby further contributing to the reduction of cash volatility.

Banking Services

The division will continue to work with ministries, Shared Services Bureau, Ministry of Consumer and Business Services (MCBS), Integrated Service Delivery Division and Management Board Secretariat e-Commerce Branch in designing and implementing cost-effective revenue collection and payment channels using new and existing banking services.

The division will negotiate with the federal government to move all transfer payments to Ontario to an electronic payment mechanism. This will assist Cash Management in its ability to make better forecasts, thereby resulting in greater efficiencies. This will also move the Province closer to meeting the proposed Canadian Payments Association requirement that will limit cheque payments to $25 million, effective February 3, 2003. In making the transition to electronic payments, the OFA will work with the Shared Services Bureau as well as consult with the ministries and their clients who are affected by this regulation.

The division will also issue the tenders for the settlement and custodial services supporting the OFA's bond and money market activities.

Capital Markets Treasury Division

Accounting and Settlement

The division will continue to follow accounting developments and ensure that the OFA remains current with accounting pronouncements that could potentially affect the OFA and OEFC programs.

The division will also ensure that the IFIS project is adequately supported so that the OFA can meet the IFIS implementation timetable and requirements.

A review of industry best practices regarding settlements and fiscal agency functions will be undertaken and appropriate changes will be implemented or considered.

Province of Ontario Savings Office

Responsibilities

- Offer chequing/savings accounts, short-term deposits and Guaranteed Investment Certificates to the public.
- Plan and execute the Ontario Savings Bond Campaign.

The Province of Ontario Savings Office (POSO) provides deposit-taking services to the public through a network of 23 branches, four agencies and one office. There is currently $2.6 billion in deposits, ranging from demand deposits paying daily interest, to five-year guaranteed investment certificates. Deposits made at POSO offer depositors the same security as that provided to a holder of the Province's bonds.

2001-02 Accomplishments

POSO is responsible for the planning and delivery of the Ontario Savings Bond campaign. In 2001, Ontario reached another record for provincial bond issues, the largest in Canadian history with $4.2 billion in sales.

On May 9, 2001, then Minister of Finance James Flaherty announced that the Ontario government will be seeking a buyer for POSO. The Government anticipates that the sale of POSO will be completed during fiscal 2002-03. Clients and POSO employees will be kept advised of developments throughout the sale process.

Priorities for 2002-03

In 2002, POSO will manage the eighth annual Ontario Savings Bond campaign. As savings bonds are aimed at the small retail investor, the goal this year will be to increase the proportion of bonds sold to smaller investors through traditional retail outlets.

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Financial Statements

Summary of Financial Results

Responsibility for Financial Reporting

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Balance Sheet

Statement of Net Income and Retained Earnings

Cash Flow Statement

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Summary of Financial Results

The OFA's main source of revenue continues to be derived from the operations of the Province of Ontario Savings Office (POSO), which accepts deposits from the general public. The OFA operates POSO as an agent of the Minister of Finance and POSO deposits are direct liabilities of the Consolidated Revenue Fund.

Total funds on deposit with POSO as of March 31, 2002 were $2.56 billion, representing an increase of $20 million from the $2.54 billion reported as of March 31, 2001. Year over year, an increase in deposit by government agencies of $92 million and long-term GIC deposits of $51 million was offset by a decrease in short term-funds on deposit by the general public of $123 million.

The average effective rate of interest paid on all POSO deposits for the year ended March 31, 2002 decreased to 3.40 per cent from 4.25 per cent for the same period last year. The decrease is a reflection of the general fall in interest rates compared to last year.

OFA's net income for the year ended March 31, 2002 was $7.4 million, a decrease of $3.7 million from the $11.1 million reported for the same period last year. This is largely due to a decrease in POSO net interest earned of $5.3 million as falling interest rates resulted in lower interest rate spreads, partially offset by an increase in POSO miscellaneous revenue of $700,000 and lower POSO operating costs of $800,000.

Salaries, wages and benefits totalling $17.1 million represent a decrease of $800,000 over last year primarily due to lower benefit costs.

Net capital assets as of March 31, 2002 were $1.7 million, representing a balance as of April 1, 2001 of $1.8 million plus purchases of $1.1 million and less amortization of $1.2 million. Purchases pertained mainly to computer workstation and technology infrastructure upgrades required for specialized financial applications.

Retained earnings of $74 million (since inception) represent notional amounts. Annually, the OFA's financial results are consolidated on a line-by-line basis with those of the Province. This accounting treatment is in accordance with the Public Sector Accounting Board (PSAB) of the CICA, under which the OFA is considered a government organization.

As agent for the Province, the OFA made loans to public bodies, the repayment of which is to be funded through third-party revenues. These loans are reported in Note 5 to the financial statements. They include loans made to the Metro Toronto Convention Centre for expansion of its facilities, the Ontario Northland Transportation Commission for the acquisition of new lumber cars, and the Corporation of the City of Windsor for the construction of the Windsor Justice Facility.

The outstanding balance of these loans, including capitalized interest, as of March 31, 2002 was $217 million. The net decrease of $5 million (from the $222 million reported a year ago) is due to repayments of $9.6 million, $1.8 million and $600,000 made by the Metro Toronto Convention Centre, the Ontario Northland Transportation Commission and Centennial Centre of Science and Technology, respectively, partially offset by interest capitalization.

The OFA continued to provide investment management services to the Northern Ontario Heritage Fund Corporation, Ontario Trillium Foundation and Ontario Securities Commission. As of March 31, 2002, the OFA managed investments of $257 million, $90 million, and $20 million respectively on their behalf (March 31, 2001 - $224 million, $101 million and $20 million respectively).

The OFA also administers the loans receivable and payable of the former Ontario Municipal Improvement Corporation (OMIC). OMIC assets of $79 million consist of debentures receivable from various municipalities and school boards. An equal amount of liabilities are payable to Canada Pension Plan and the Province. During the 2001-02 year, approximately $297,000 of loans receivable from municipalities matured. The interest earned and paid annually on account of OMIC assets and liabilities amounts to $7.6 million and is expected to remain at this level until 2011, when CPP loans start maturing.

Responsibility for Financial Reporting

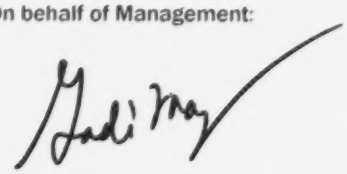
The accompanying financial statements of the Ontario Financing Authority have been prepared in accordance with accounting principles generally accepted in Canada and are the responsibility of management. The preparation of financial statements necessarily involves the use of estimates based on management's judgement, particularly when transactions affecting the current accounting period cannot be finalized with certainty until future periods. The financial statements have been properly prepared within reasonable limits of materiality and in light of information available up to June 28, 2002.

Management maintains a system of internal controls designed to provide reasonable assurance that the assets are safeguarded and that reliable financial information is available on a timely basis. The system includes formal policies and procedures and an organizational structure that provides for appropriate delegation of authority and segregation of responsibilities. An internal audit function independently evaluates the effectiveness of these internal controls on an ongoing basis and reports its findings to management and the Audit Committee of the Board of Directors.

The Board of Directors, through the Audit Committee, is responsible for ensuring that management fulfils its responsibilities for financial reporting and internal controls. The Audit Committee meets periodically with management, the internal auditors, and the external auditor to deal with issues raised by them and to review the financial statements before recommending approval by the Board of Directors.

The financial statements have been audited by the Provincial Auditor. The Provincial Auditor's responsibility is to express an opinion on whether the financial statements are fairly presented in accordance with Canadian generally accepted accounting principles. The Auditor's Report, which appears on the following page, outlines the scope of the Auditor's examination and opinion.

On behalf of Management:



Gadi Mayman
CEO and Vice-Chair (Interim)
Ontario Financing Authority
June 28, 2002

Auditor's Report

Office of the
Provincial Auditor
of Ontario

Bureau du
vérificateur provincial
de l'Ontario

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(416) 327-2381 Fax: (416) 327-9862

Auditor's Report

To the Ontario Financing Authority
and to the Minister of Finance

I have audited the balance sheet of the Ontario Financing Authority as at March 31, 2002 and the statement of net income and retained earnings, and the cash flow statement for the year then ended. These financial statements are the responsibility of the Authority's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with Canadian generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Authority as at March 31, 2002 and the results of its operations and its cash flows for the year then ended, in accordance with Canadian generally accepted accounting principles.

Erik Peters

Toronto, Ontario
June 28, 2002

Erik Peters, FCA
Provincial Auditor

Balance Sheet

As at March 31, 2002

(in thousands of dollars)	Corporate	POSO	Total 2002	restated (note8) Total 2001
ASSETS				
Current assets				
Cash	$ 134	21,733	**21,867**	$ 13,573
Receivable from the Province of Ontario (note 2i and 8ii)	—	2,108,550	**2,108,550**	2,139,691
Accounts receivable	4,576	34,876	**39,452**	46,801
Loans receivable (note 4)	9	—	**9**	301
Total current assets	$ 4,719	2,165,159	**2,169,878**	$2,200,366
Long-term assets				
Capital assets (note 3)	1,410	323	**1,733**	1,785
Receivable from the Province of Ontario (note 2ii)	—	497,058	**497,058**	446,194
Loans receivable (note 4)	79,038	—	**79,038**	79,043
Total assets	**$85,167**	2,662,540	2,747,707	**$2,727,388**
LIABILITIES AND RETAINED EARNINGS				
Current liabilities				
Accounts payable and accrued liabilities	$ 6,077	30,670	**36,747**	$ 43,779
Funds on deposit (note 2i)	—	2,060,865	**2,060,865**	2,091,494
Due to the Province of Ontario (note 4)	9	—	**9**	301
Total current liabilities	$ 6,086	2,091,535	**2,097,621**	$2,135,574
Long-term debt				
Funds on deposit (note 2ii)	—	497,058	**497,058**	446,194
Due to CPP and the Province of Ontario (note 4)	79,048	—	**79,048**	79,053
Total liabilities	$85,134	2,588,593	**2,673,727**	$2,660,821
Retained earnings	33	73,947	**73,980**	66,567
Total liabilities and retained earnings	**$85,167**	2,662,540	2,747,707	**$2,727,388**

See accompanying notes to financial statements.

Approved on behalf of the Board:

Bob Christie
Chair

Michael L. Gourley
Vice-Chair and Chief Executive Officer

Statement of Net Income and Retained Earnings

Year ended March 31, 2002

(in thousands of dollars)	Corporate	POSO	**Total 2002**	restated (note8) Total 2001
REVENUE				
Interest revenue	$ 7,607	105,392	**112,999**	$ 145,361
Cost recovery from the Province	11,770	—	**11,770**	11,494
Miscellaneous revenue	—	1,497	**1,497**	821
Total revenue	**$ 19,377**	**106,889**	**126,266**	**$ 157,676**
EXPENDITURES				
Interest on short-term debt	$ —	59,411	**59,411**	$ 89,560
Interest on long-term debt	7,601	27,275	**34,876**	31,803
Salaries, wages and benefits	8,692	8,434	**17,126**	17,891
Administrative and general	2,233	4,041	**6,274**	6,213
Amortization	845	321	**1,166**	1,112
Total expenditures	**$ 19,371**	**99,482**	**118,853**	**$ 146,579**
Net income for the year	$ 6	7,407	**7,413**	$ 11,097
Retained earnings, beginning of the year	27	66,540	**66,567**	55,470
Retained earnings, end of the year	$ 33	73,947	**73,980**	$ 66,567

See accompanying notes to financial statements.

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Total current liabilities	$ 6,086	2,091,535	**2,097,621**	$2,135,574
Long-term debt				
Funds on deposit (note 2ii)	—	497,058	**497,058**	446,194
Due to CPP and the Province of Ontario (note 4)	79,048	—	**79,048**	79,053
Total liabilities	$85,134	2,588,593	**2,673,727**	$2,660,821
Retained earnings	33	73,947	**73,980**	66,567
Total liabilities and retained earnings	**$85,167**	**2,662,540**	**2,747,707**	**$2,727,388**

See accompanying notes to financial statements.

Approved on behalf of the Board:

Bob Christie
Chair

Michael L. Gourley
Vice-Chair and Chief Executive Officer

Statement of Net Income and Retained Earnings

Year ended March 31, 2002

(in thousands of dollars)	Corporate	POSO	**Total 2002**	restated (note 8) Total 2001
REVENUE				
Interest revenue	$ 7,607	105,392	**112,999**	$ 145,361
Cost recovery from the Province	11,770	—	**11,770**	11,476
Miscellaneous revenue	—	1,497	**1,497**	839
Total revenue	**$ 19,377**	**106,889**	**126,266**	**$ 157,676**
EXPENDITURES				
Interest on short-term debt	$ —	59,411	**59,411**	$ 89,536
Interest on long-term debt	7,601	27,275	**34,876**	31,697
Salaries, wages and benefits	8,692	8,434	**17,126**	17,901
Administrative and general	2,233	4,041	**6,274**	6,217
Amortization	845	321	**1,166**	1,111
Total expenditures	**$ 19,371**	**99,482**	**118,853**	**$ 146,579**
Net income for the year	$ 6	7,407	**7,413**	$ 11,097
Retained earnings, beginning of the year	27	66,540	**66,567**	55,470
Retained earnings, end of the year	$ 33	73,947	**73,980**	$ 66,567

See accompanying notes to financial statements.

Cash Flow Statement

Year ended March 31, 2002

(millions of dollars)	Corporate	POSO	Total 2002	restated (note8) Total 2001
Cash flows from operating activities				
Net income for the year	$ 6	7,407	**7,413**	$ 11,097
Adjustments to reconcile net income to funds provided by operating activities:				
Amortization	845	321	**1,166**	1,112
Net change in receivables, payable and accrued liabilities	236	(20)	**216**	(32)
Cash flows from operating activities	**$ 1,087**	**7,708**	**8,795**	**$ 12,177**
Cash flows from financing activities				
Increase (decrease) in proceeds from depositors	$ —	20,235	**20,235**	$ (274,485)
Repayments to the Province re: OMIC loans	(297)	—	**(297)**	(487)
Repayments from holders of OMIC loans	297	—	**297**	487
Cash flows from/(used in) financing activities	**$ —**	**20,235**	**20,235**	**$ (274,485)**
Cash flows from investing activities				
Transfer of POSO funds from (to) the Province of Ontario	$ —	(19,623)	**(19,623)**	$ 254,022
Purchase of capital assets	(1,082)	(31)	**(1,113)**	(875)
Cash flows (used in)/from investing activities	**$(1,082)**	**(19,654)**	**(20,736)**	**$ 253,147**
Net increase (decrease) in cash	$ 5	8,289	**8,294**	$ (9,161)
Cash at beginning of the year	129	13,444	**13,573**	22,734
Cash at end of the year	**$ 134**	**21,733**	**21,867**	**$ 13,573**

See accompanying notes to financial statements.

Notes to Financial Statements for the Year Ended March 31, 2002

(all tables are in thousands of dollars)

Background

The Ontario Financing Authority (the "OFA") was established as an agency of the Crown, on November 15, 1993, by the *Capital Investment Plan Act, 1993* (the "Act"). In accordance with the Act, the OFA's objects are:

- to assist public bodies and the Province of Ontario to borrow and invest money;
- to develop and carry out financing programs, issue securities, and manage cash, currency and other financial risks on behalf of the Province, or any public body;
- to provide such other financial services as are considered advantageous to the Province or any public body;
- to operate offices as provided under the *Province of Ontario Savings Office Act*, as agent for the Minister of Finance; and
- any additional objects as directed by the Lieutenant Governor in Council.

The OFA is a corporation established under the laws of Ontario. The OFA is exempt from federal and provincial income taxes under paragraph 149(1)(d) of the *Income Tax Act* of Canada.

1 Significant Accounting Policies

(i) General. The financial statements are prepared in accordance with Canadian generally accepted accounting principles prescribed by the Canadian Institute of Chartered Accountants.

(ii) Capital assets. Capital assets are stated at cost. Amortization is provided using the straight-line method over the estimated useful life of the asset as listed below, starting in the year of acquisition i.e., half year depreciation is charged in the year of acquisition and half year in the year of disposal, irrespective of the date of acquisition or disposal.

Furniture and equipment	5 years
Computer hardware	3 years
Leasehold improvements	remaining life of lease

2 Province of Ontario Savings Office

The OFA operates the Province of Ontario Savings Office (POSO) as agent of the Minister of Finance. POSO accepts deposits from the general public, government and other public bodies that form part of the Consolidated Revenue Fund and are direct liabilities of the Province. In the May 9, 2001 Budget, the Minister of Finance announced that the Government would be seeking a buyer for the Province of Ontario Savings Office (POSO). POSO's sale is overseen by the Ontario SuperBuild Corporation.

Administration costs for the period ended March 31, 2002 of $1,100,526 (March 31, 2001 - $992,066) relating to POSO are provided by the Ministry of Finance and are not included in these financial statements. The average rate of interest paid to depositors and earned from the Province for the year ended March 31, 2002 was 3.40 per cent and 4.06 per cent respectively (March 31, 2001 was 4.25 per cent and 5.08 per cent respectively). These deposits are comprised as follows:

Summary of funds on deposit by general public and government agencies

	As at March 31, 2002			As at March 31, 2001	
	General Public	Government Agencies	Total	General Public	Government Agencies
Short-term deposits	$ 158,196	123,000	$ 281,196	$ 83,911	[illegible]
Demand deposits	1,042,250	175,513	1,217,763	1,044,268	[illegible]
GICs maturing within one year	561,906	-	561,906	756,825	[illegible]
Total short-term funds	$ 1,762,352	298,513	$ 2,060,865	$ 1,885,004	[illegible]
Long-term funds	497,058	-	497,058	446,194	[illegible]
Total funds on deposit	$ 2,259,410	298,513	$ 2,557,923	$ 2,331,198	[illegible]

Cash Flow Statement

Year ended March 31, 2002

(in thousands of dollars)	Corporate	POSO	Total 2002	restated (note8) Total 2001
Cash flows from operating activities				
Net income for the year	$ 6	7,407	**7,413**	$ 11,097
Adjustments to reconcile net income to funds provided by operating activities:				
Amortization	845	321	**1,166**	1,112
Net change in receivables, payable and accrued liabilities	236	(20)	**216**	(32)
Cash flows from operating activities	**$ 1,087**	**7,708**	**8,795**	**$ 12,177**
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Increase (decrease) in proceeds from depositors	$ —	20,235	**20,235**	$ (274,485)
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Cash flows from investing activities				
Transfer of POSO funds from/(to) the Province of Ontario	$ —	(19,623)	**(19,623)**	$ 254,022
Purchase of capital assets	(1,082)	(31)	**(1,113)**	(875)
Cash flows (used in)/from investing activities	**$(1,082)**	**(19,654)**	**(20,736)**	**$ 253,147**
Net increase (decrease) in cash	$ 5	8,289	**8,294**	$ (9,161)
Cash at beginning of the year	129	13,444	**13,573**	22,734
Cash at end of the year	**$ 134**	**21,733**	**21,867**	**$ 13,573**

See accompanying notes to financial statements.

Notes to Financial Statements for the Year Ended March 31, 2002

(all tables are in thousands of dollars)

Background

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- to develop and carry out financing programs, issue securities, and manage cash, currency and other financial risks on behalf of the Province, or any public body;
- to provide such other financial services as are considered advantageous to the Province or any public body;
- to operate offices as provided under the *Province of Ontario Savings Office Act*, as agent for the Minister of Finance; and
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Furniture and equipment	5 years
Computer hardware	3 years
Leasehold improvements	remaining life of lease

2. Province of Ontario Savings Office

The OFA operates the Province of Ontario Savings Office (POSO) as agent of the Minister of Finance. POSO accepts deposits from the general public, government and other public bodies that form part of the Consolidated Revenue Fund and are direct liabilities of the Province. In the May 9, 2001 Budget, the Minister of Finance announced that the Government would be seeking a buyer for the Province of Ontario Savings Office (POSO). POSO's sale is overseen by the Ontario SuperBuild Corporation.

Administration costs for the period ended March 31, 2002 of $1,100,526 (March 31, 2001 - $992,066) relating to POSO are provided by the Ministry of Finance and are not included in these financial statements. The average rate of interest paid to depositors and earned from the Province for the year ended March 31, 2002 was 3.40 per cent and 4.06 per cent respectively (March 31, 2001 was 4.25 per cent and 5.08 per cent respectively). These deposits are comprised as follows:

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	As at March 31, 2002			As at March 31, 2001		
	General Public	Government Agencies	Total	General Public	Government Agencies	Total
Short-term deposits	$ 158,196	123,000	$ 281,196	$ 83,911	117,000	$ 200,911
Demand deposits	1,042,250	175,513	1,217,763	1,044,268	89,490	1,133,758
GICs maturing within one year	561,906	-	561,906	756,825	-	756,825
Total short-term funds	$ 1,762,352	298,513	$ 2,060,865	$ 1,885,004	206,490	$ 2,091,494
Long-term funds	497,058	-	497,058	446,194	-	446,194
Total funds on deposit	$ 2,259,410	298,513	$ 2,557,923	$ 2,331,198	206,490	$ 2,537,688

Notes to Financial Statements

(ii) Receivable from the Province of Ontario and short-term funds on deposit

The total current 'Receivable from the Province' of $2,108,550 (March 31, 2001 - $2,139,691) includes short-term funds on deposit plus working capital.

(iii) Receivable from the Province of Ontario and long-term funds on deposit

The long-term 'Receivable from the Province' represents deposits for which POSO has issued long-term GICs. These deposits mature as follows:

	As at March 31, 2002		As at March 31, 2001	
Year ended March 31	Principal Maturing	Effective Average Interest Rate (%)	Principal Maturing	Effective Average Interest Rate (%)
2003	$ —		$ 212,708	5.65
2004	173,718	4.72	87,599	5.53
2005	152,250	5.40	99,072	5.95
2006	62,461	5.57	46,815	5.92
2007	108,629	5.04	—	
Total	**$ 497,058**		**$ 446,194**	

3 Capital Assets

The balance of capital assets, net of amortization, is as follows:

	Cost	Accumulated Amortization	Net March 31, 2002	Net March 31, 2001
Furniture and equipment	$ 1,218	$ (1,120)	$ 98	$ 115
Computer hardware	6,242	(5,006)	1,236	1,475
Leasehold improvement	1,613	(1,214)	399	195
Total	**$ 9,073**	**$ (7,340)**	**$ 1,733**	**$ 1,785**

4 Ontario Municipal Improvement Corporation (OMIC)

In accordance with the *Capital Investment Plan Act, 1993*, the Ontario Municipal Improvement Corporation (OMIC) ceased to exist and its assets and liabilities were transferred to the OFA on November 15, 1993. OMIC received loans from the Canada Pension Plan (CPP) and the Province, which OMIC used to make loans to municipalities and school boards under similar terms as its debt.

As of March 31, 2002, the portion of long-term debt maturing in 2002-03 is $9,000 (March 31, 2001 - $301,000 maturing in 2001-02) and is due to the Province. Long-term debt (maturing in the year ended March 31, 2004 and future) is comprised of debt due to the Province of $27,000 and to the Canada Pension Plan of $79 million (March 31, 2001 - $32,000 and $79 million respectively, maturing in year ended March 31, 2003 and future). The terms of the outstanding debt are as follows:

	As at March 31, 2002		As at March 31, 2001	
Year ended March 31	Principal Maturing	Effective Average Interest Rate (%)	Principal Maturing	Effective Average Interest Rate (%)
2002	$ —		$ 301	13.95
2003	9	11.25	5	11.25
2004	5	11.25	5	11.25
2005	6	11.25	6	11.25
2006	6	11.25	6	11.25
2007	—		—	
1 - 5 years	$ 26		$ 323	
6 - 20 years	79,031	9.61	79,031	9.61
Total	**$ 79,057**		**$ 79,354**	

5. Transactions With the Province and Other Public Bodies

(i) Financing activities between the Province and other Public Bodies: Acting as a financial conduit for the Province, the OFA provides financing to various public bodies, the repayment of which is expected from third-party revenues. The funds for these loans are advanced to the OFA by the Province under a credit facility of $2.16 billion. Repayments received from public bodies by the OFA are forwarded to the Province. These transactions are not reflected in these financial statements.

In compliance with an Ontario Financing Authority Lending Policy adopted by its Board of Directors on December 17, 1997, each advance received by the OFA under the current facility bears interest at a rate that is equivalent to the rate of interest payable to the OFA on the corresponding loan to a public body(ies). As of March 31, 2002, $217 million (March 31, 2001 - $222 million), including accrued interest, was advanced by the Province to the OFA and must be repaid by the OFA on or before August 31, 2027.

Funds are generally advanced by the OFA to public bodies under interim financing arrangements, consisting of a number of promissory notes for terms not exceeding one year. Interest is payable on the principal plus any capitalized interest. As of March 31, 2002, interest rates on these promissory notes ranged from 2.2 per cent to 2.4 per cent (March 31, 2001 from 4.50 per cent to 5.60 per cent). It is the OFA's intention to replace these promissory notes with term debt, at which point repayment terms will be finalized.

Prior to March 31, 2002, the original amounts of promissory notes converted into debentures were as follows: Ontario Northland Transportation Commission - $3.9 million at 5.64 per cent maturing April 1, 2008; $12.7 million at 6.37 per cent maturing August 1, 2014; $19 million at 5.6 per cent maturing December 1, 2014. City of Windsor - $26.4 million at 6.41 per cent maturing March 31, 2021.

The following represents amounts receivable by the OFA on behalf of the Province, including capitalized interest. These are related party transactions, with the exception of those with the City of Windsor.

Notes to Financial Statements

Receivable from the Province of Ontario and short-term funds on deposit

The total current 'Receivable from the Province' of $2,108,550 (March 31, 2001 - $2,139,691) includes short-term funds on deposit plus working capital.

Receivable from the Province of Ontario and long-term funds on deposit

The long-term 'Receivable from the Province' represents deposits for which POSO has issued long-term GICs. These deposits mature as follows:

	As at March 31, 2002		As at March 31, 2001	
Year ended March 31	Principal Maturing	Effective Average Interest Rate (%)	Principal Maturing	Effective Average Interest Rate (%)
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2004	173,718	4.72	87,599	5.53
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2004	5	11.25	5	11.25
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2007	—		—	
1 - 5 years	$ 26		$ 323	
6 - 20 years	79,031	9.61	79,031	9.61
Total	**$ 79,057**		**$ 79,354**	

5 Transactions With the Province and Other Public Bodies

(a) Financing activities between the Province and other Public Bodies. Acting as a financial conduit for the Province, the OFA provides financing to various public bodies, the repayment of which is expected from third party revenues. The funds for these loans are advanced to the OFA by the Province under a credit facility of $2.16 billion. Repayments received from public bodies by the OFA are forwarded to the Province. These transactions are not reflected in these financial statements.

In compliance with an Ontario Financing Authority Lending Policy adopted by its Board of Directors on December 17, 1997, each advance received by the OFA under the current facility bears interest at a rate that is equivalent to the rate of interest payable to the OFA on the corresponding loan to a public bodyries). As of March 31, 2002, $217 million (March 31, 2001 - $222 million), including accrued interest, was advanced by the Province to the OFA and must be repaid by the OFA on or before August 31, 2027.

Funds are generally advanced by the OFA to public bodies under interim financing arrangements consisting of a number of promissory notes for terms not exceeding one year. Interest is payable on the principal plus any capitalized interest. As of March 31, 2002, interest rates on these promissory notes ranged from 2.2 per cent to 2.4 per cent (March 31, 2001 from 4.50 per cent to 5.60 per cent). It is the OFA's intention to replace these promissory notes with term debt, at which point repayment terms will be finalized.

Prior to March 31, 2002, the original amounts of promissory notes converted into debentures were as follows: Ontario Northland Transportation Commission - $3.9 million at 5.64 per cent maturing April 1, 2008, $12.7 million at 6.37 per cent maturing August 1, 2014, $19 million at 5.6 per cent maturing December 1, 2014. City of Windsor - $26.4 million at 6.41 per cent maturing March 31, 2021.

The following represents amounts receivable by the OFA on behalf of the Province, including capitalized interest. These are related party transactions, with the exception of those with the City of Windsor.

	March 31, 2002	March 31, 2001
Metro Toronto Convention Centre	$ 158,086	$ 161,726
Ontario Northland Transportation Commission	31,133	32,977
Corporation of the City of Windsor	28,110	26,416
Centennial Centre of Science and Technology	-	608
	$ 217,329	$ 221,727

The Metro Toronto Convention Centre Corporation (MTCC) is a Crown agency of the Province under the *Metropolitan Toronto Convention Centre Corporation Act*. The majority of directors on the MTCC board are appointed by the Lieutenant Governor in Council.

The Ontario Northland Transportation Commission (ONTC) is a Crown agency of the Province under the *Ontario Northland Transportation Commission Act, 1990*. Members of the Commission are appointed by the Lieutenant Governor in Council.

The Corporation of the City of Windsor is a municipality within the meaning of the *Municipal Act*. The financing provided is for the acquisition, design and construction of the Windsor Justice Facility, consisting of provincial division courthouse and city police headquarters.

The Centennial Centre of Science and Technology is a Crown agency of the Province under the *Centennial Centre of Science and Technology Act*. Its Board of Trustees is appointed by the Lieutenant Governor in Council.

(ii) Investing for Related Parties. In the normal course of operations, the OFA provides investment management services to other public bodies. Funds managed on behalf of other public bodies (which are not reflected in these financial statements) as of March 31, 2002, consist of $257 million managed on behalf of the Northern Ontario Heritage Fund Corporation (March 31, 2001 - $224 million), $90 million managed on behalf of Ontario Trillium Foundation (March 31, 2001 - $101 million) and $20 million managed on behalf of Ontario Securities Commission (March 31, 2001 - $20 million). The OFA also manages debt on behalf of the Province and was reimbursed $11.7 million for the year ended March 31, 2002 for these activities (March 31, 2001 - $11.5 million).

(iii) Province of Ontario Savings Office: Other related parties have deposited their funds on a short-term basis. Total amounts deposited as at March 31, 2002 were $299 million (March 31, 2001 - $206 million).

6. Pension Plan

The OFA provides pension benefits to its full-time employees through participation in the Public Service Pension Plan, which is a multi-employer defined benefit plan. This plan is accounted for as a defined contribution plan, as the OFA has insufficient information to apply defined benefit plan accounting to this pension plan.

The OFA's pension contributions for the period ended March 31, 2002 were $614,000 (March 31, 2001 - $733,000). The cost of post-retirement, non-pension employee benefits are paid by Management Board Secretariat and are not included in the above figures.

7. Financial Instruments

The carrying amounts for cash, accounts receivable, receivable from the Province of Ontario, accounts payable and accrued liabilities and short-term funds on deposit approximate their fair values because of the short-term maturity of these instruments.

Given that the terms and amounts of the OFA's long-term receivables offset the OFA's long-term debt, providing fair values for these instruments would not add any more useful information to that which has already been presented in these financial statements.

8. Restatement of Comparative Figures

(i) Capital assets - change in accounting policy: During the year the OFA changed its accounting policy for amortization of assets. In prior years, amortization of assets began in the year following the year of acquisition. During the year, OFA adopted the policy of "Partial Year Amortization" (Half Year Rule) whereby amortization is charged for half year in the year of acquisition and half year in the year of disposal, irrespective of the date of acquisition or disposal. OFA has retroactively applied this policy and prior year figures have been restated. As a result of the change, the fiscal year 2000-01 capital assets, net income and retained earnings decreased by $135,000.

(ii) Restatement for adjustment of receivable from the Province: At the time of termination of loans-based financing in 1996, when most of the loans to capital corporations were written off, an adjustment to write off a receivable of $414,000 from the Province for profit earned due to spread on these on-lending activities by the OFA, should have been reflected in the same year. This correction has been adjusted on a retroactive basis. As a result, opening retained earnings at April 1, 2000 and receivable from the Province as at that date decreased by $414,000.

The effect of these adjustments is as follows:

	2001		
	Previously Stated	Change (Reduction)	Restated
Receivables from the Province of Ontario	$ 2,140,105	$ (414)	$ 2,139,691
Capital Assets	1,920	(135)	1,785
Net Income for the year	11,232	(135)	11,097
Retained Earnings	67,116	(549)	66,567

9. Contingencies

The Province of Ontario Savings Office is from time to time involved in various legal proceedings arising out of the ordinary course and conduct of business. Settlements, if any, concerning these contingencies will be accounted for in the period in which the settlement occurs. The outcome and ultimate disposition of these actions are not determinable at this time.

10. Comparative Figures

Certain of the 2000-01 comparative figures have been reclassified to conform with the financial statement presentation adopted in 2001-02.

	March 31, 2002	March 31, 2001
Metro Toronto Convention Centre	$ 158,086	$ 161,726
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The carrying amounts for cash, accounts receivable, receivable from the Province of Ontario, accounts payable and accrued liabilities and short-term funds on deposit approximate their fair values because of the short-term maturity of these instruments.

Given that the terms and amounts of the OFA's long-term receivables offset the OFA's long-term debt, providing fair values for these instruments would not add any more useful information to that which has already been presented in these financial statements.

8. Restatement of Comparative Figures

(i) Capital assets - change in accounting policy: During the year the OFA changed its accounting policy for amortization of assets. In prior years, amortization of assets began in the year following the year of acquisition. During the year, OFA adopted the policy of "Partial Year Amortization" (Half Year Rule) whereby amortization is charged for half year in the year of acquisition and half year in the year of disposal, irrespective of the date of acquisition or disposal. OFA has retroactively applied this policy and prior year figures have been restated. As a result of the change, the fiscal year 2000-01 capital assets, net income and retained earnings decreased by $135,000.

(ii) Restatement for adjustment of receivable from the Province: At the time of termination of loans-based financing in 1996, when most of the loans to capital corporations were written off, an adjustment to write off a receivable of $414,000 from the Province for profit earned due to spread on these on-lending activities by the OFA, should have been reflected in the same year. This correction has been adjusted on a retroactive basis. As a result, opening retained earnings at April 1, 2000 and receivable from the Province as at that date decreased by $414,000.

The effect of these adjustments is as follows:

	2001		
	Previously Stated	Change (Reduction)	Restated
Receivables from the Province of Ontario	$ 2,140,105	$ (414)	$ 2,139,691
Capital Assets	1,920	(135)	1,785
Net Income for the year	11,232	(135)	11,097
Retained Earnings	67,116	(549)	66,567

9. Contingencies

The Province of Ontario Savings Office is from time to time involved in various legal proceedings arising out of the ordinary course and conduct of business. Settlements, if any, concerning these contingencies will be accounted for in the period in which the settlement occurs. The outcome and ultimate disposition of these actions are not determinable at this time.

10. Comparative Figures

Certain of the 2000-01 comparative figures have been reclassified to conform with the financial statement presentation adopted in 2001-02.

Notes to Financial Statements

11. Salaries (absolute dollars)

The *Public Sector Salary Disclosure Act, 1996*, requires disclosure of Ontario Public-sector employees paid remuneration (e.g. salary, performance-based pay and severance) during the year in excess of $100,000. The amounts paid to such individuals in 2001 are as listed below:

Name	Position	Remuneration Paid	Taxable Benefits
Charles Allain	Director - Debt Management	$170,480	$ 315
Ken Broadbent	Manager - Foreign Exchange	$109,612	$ 221
José Ignacio Campos	Director - Risk Control	$131,499	$ 298
Kanak Chopra	Director - Risk Control (Previous)	$157,829	$ 269
James Devine	Manager - Medium-Term Notes & Private Placements	$151,943	$ 301
Andrew Hainsworth	Manager - Funding	$151,957	$ 301
John Logie	Manager - Financial Engineering	$111,782	$ 221
Michael Manning	Executive Director - Capital Markets	$227,786	$ 421
Gadi Mayman	Vice Chair & CEO (Interim), OFA	$275,688	$ 560
Christine Moszynski	Director - Capital Markets Treasury	$119,852	$ 263
David Peters	Manager - Derivatives	$151,957	$ 301
William Ralph	Director - Corporate Finance	$138,940	$ 289
Ken Russell	Legal Counsel	$157,081	$ 313
Tony Salerno	Vice Chair & CEO, OFA (Previous)	$634,642	$5,790
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Corporate Governance

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Corporate Policies

Corporate Governance

Corporate governance at the Ontario Financing Authority involves processes that permit the effective supervision and management of the OFA's activities by its senior management, the Board of Directors and the Minister of Finance. It includes identifying those individuals and groups who are responsible for the OFA's activities and specifying their roles.

The Ontario Financing Authority's accountability framework flows from its governing statute, the *Capital Investment Plan Act, 1993* and from a Memorandum of Understanding between OFA and the Minister of Finance. Together, they provide that the Minister of Finance is accountable to Cabinet for the activities of OFA. The Chief Executive Officer reports to the Board of Directors. In turn, the Board reports to the Minister of Finance.

The Minister of Finance supervises the OFA with the aid of information reported through the Chair of the Board of Directors, who is also the Deputy Minister of Finance, and through senior management of the OFA. The Minister of Finance reviews and approves the OFA's annual business plan, which contains long- and short-term objectives and reports on accomplishments for the preceding year. In keeping with the government's Agency Establishment and Accountability Directive, once every three years the Minister of Finance recommends the OFA business plan to Management Board of Cabinet for approval.

The Chief Executive Officer (CEO) is responsible to the Board of Directors for day-to-day operations. The CEO also ensures that policies and procedures, including financial reporting, remain relevant and effective. Staff are accountable, through senior management, to the CEO.

Corporate Policies

The *Capital Investment Plan Act, 1993* sets out a broad framework for Ontario Financing Authority's operations. This is supplemented by a memorandum of understanding with the Minister of Finance and internal policies including financial reporting.

In carrying out its mandate, the Ontario Financing Authority faces financial risks that are inherent in managing financial assets and liabilities. Risk management policies ensure that these risks are identified, monitored, evaluated, reported and managed. The OFA manages financial risk through a comprehensive framework of debt management infrastructure, policies and procedures.

Overview and Structure

Board of Directors

- Reviews and approves key risk management policies.
- Supervises the management of the Province's debt and investment portfolio.

Audit Committee

- Oversees the financial reporting process on behalf of the Board of Directors.
- Reviews key risk management policies, internal audit reports and the financial statements.

Management Committees

Risk Management Committee

- Reviews daily market updates and outlook.
- Reviews current borrowing, investing and debt management positions and strategies.

Borrowing Strategy Committee

- Reviews economic conditions, fiscal plan and capital markets outlook.
- Reviews borrowing and debt management activities and management reports, cash flows and the public debt interest forecast.
- Reviews operational limits and procedures related to financial operations.
- Approves amendments and exceptions to approved risk management policies and procedures.
- Approves risk management policies for recommendation to the Board of Directors.

Risk Control Division

- Monitors, measures and assesses and reports upon financial market and counterparty risks and performance associated with borrowing, debt management and investment of liquid reserves.
- Reports on a regular and timely manner to the Board of Directors and senior OFA management on the status of the Province's financial market activities, associated exposures and compliance with approved policies.
- Develops risk management policies in line with "best" industry practices in an evolving business environment and monitors compliance with Board-approved policies, limits and procedures, and monitors portfolio performance and trends.
- Assesses counterparty credit risk and manages rating agency relations.

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Corporate Policies

Risk Management Policy Framework

The Ontario Financing Authority has a number of policies in place to minimize financial risk: market risk, credit risk, operational risk, supply availability risk and risks related to the use of derivatives. These policies were developed after reviewing the Group of Thirty's best practices, the guidelines and directives of regulatory bodies, such as the Office of the Superintendent of Financial Institutions of Canada, the Bank for International Settlements (BIS), and consulting with Canadian bank representatives on their risk management practices. Key aspects of the policies are summarized below.

A. Market Risk

Market Risk is the financial loss attributable to changes in the values of financial indices including interest rates, credit spreads, foreign exchange and liquidity risk.

The market risk policy provides a framework for borrowing and integrates several aspects dealing with the management of market risk. Among the provisions are:

- Foreign Exchange Limit - The Province's exposure to unhedged foreign currency is limited to 5 per cent of outstanding debt. Foreign-currency exchange exposures are limited to Group of Seven currencies and the Swiss franc or equivalent currencies (i.e., Euro).
- Interest Rate Resetting Risk - Interest rate resetting risk is the combination of net floating exposure (i.e., gross floating rate exposure less liquid reserves) and all fixed rate debt to be refinanced within the next 12-month period. The Province is limited to a maximum interest rate reset exposure of 25 per cent of debt.
- Public Debt Interest and Debt Management Loss Limits - Actual Public Debt Interest (PDI) must not exceed budgeted annual PDI by more than three per cent as a result of adverse floating rate interest or foreign exchange movements (PDI loss limit). In addition, the CEO establishes a debt management trigger level to ensure that losses will not reach the PDI loss limit.
- Liquidity Risk - Liquid reserves are maintained at levels sufficient to ensure the Government can meet its short-term financial obligations. Treasury Bill and U.S. Commercial Paper programs are also available to provide liquidity should the need arise.
- Debt Maturity Profile - When issuing new debt, the OFA will aim for a smooth debt maturity profile to diversify the interest rate risk of refinancing maturing and floating rate debt.
- Risk Measurement - The Province identifies and quantifies exposures to market risk to ensure that risk exposures and losses remain within the approved exposure and loss limits. Exposure to market and credit risk is measured daily.

B. Credit Risk

Credit risk is risk that a counterparty does not meet, or defaults on, its obligations. Credit risk arises when the OFA undertakes financial and derivative transactions. The minimum credit rating of a counterparty for a new swap transaction is typically AA- and R1-mid for money market investments. The resulting exposure is capped at mark-to-market limits depending on the counterparty's credit rating.

C. Operational Risk

The Ontario Financing Authority manages operational risk through procedures that deal with model risk, legal issues, settlement issues and information systems risks.

- Model Risk - The OFA regularly reviews its pricing models for accuracy and compliance with industry standards. It also regularly reviews the valuation of financial instruments.
- Legal Risk - The OFA has established procedures and standards to ensure that documentation of debt issues, debt management and money market transactions meets industry standards and is enforceable.
- Settlement Risk - The OFA has established internal control procedures to ensure that transactions are settled correctly in a timely manner and are recorded accurately.
- Information Systems Risk - The OFA has taken measures to protect the computer systems and offices of the OFA. These include access controls to the building and work areas, monitoring the computer room environment, the establishment of a back-up power source, regular data back-ups, off-site storage, firewalls to protect against unauthorized network intrusions and computer virus scanning. Security is reviewed periodically and when major changes occur.

D. Supply Availability Risk

Supply Availability Risk is the risk associated with having to meet contractual obligations associated with portfolio hedging transactions through open market transactions. As with financial market activities, management of OEFC's NUGs electricity generation portfolio must assess both market and counterparty credit risks. In addition, managing these risks is further complicated by such risks as equipment breakdown, fuel availability and fuel costs, all of which could affect OEFC's ability to meet its contractual obligations through NUGs' supply.

E. Use of Derivatives

Derivatives are used solely to advance the OFA's objective of providing the Province's financing and liquidity requirements in a sound and cost-effective manner. Derivatives are used to manage exposures arising from existing and planned debt and in a manner consistent with the Financing and Debt Management Plans. Risks that arise from the use of derivatives are identified, monitored, evaluated and managed prudently

Corporate Policies

Risk Management Reporting

The Ontario Financing Authority's Board of Directors receives quarterly progress reports on financing and debt management plans and current risk exposures. Also, OFA management provides the Board of Directors with a monthly assessment of performance relative to benchmarks approved by the Board.

The Director of Risk Control reports to the Board of Directors on the OFA's compliance with applicable financial policies. The Deputy Minister of Finance, on behalf of the Minister of Finance, receives weekly financial and financing program reports.

The adequacy and effectiveness of internal controls are examined independently by the Audit Services Division of Management Board Secretariat. It also verifies compliance with policies, procedures and operational limits. The results of these audits are reported to management and the Audit Committee of the Board of Directors.

The OFA prepares annual financial statements in accordance with Generally Accepted Accounting Principles (GAAP) for approval by the Audit Committee and the Board of Directors. The annual financial statements are reviewed by the Provincial Auditor who expresses an opinion on whether they are presented fairly and in accordance with GAAP. The Provincial Auditor's findings are reviewed by the Audit Committee and the Board of Directors. These audited financial statements are tabled in the Ontario Legislature as part of the Ontario Financing Authority's Annual Report.

Appendix

Summary of Net Provincial Debt

Credit Ratings

Exchanges Where the Province is Listed

Sources of Information

Summary of Net Provincial Debt

NET PROVINCIAL DEBT Interim 2002[1] ($ Millions)	1998	1999	2000	2001	Interim 2002	Plan 2003
Debt Issued for Provincial Purposes [2]						
Non Public Debt						
Minister of Finance of Canada:						
Canada Pension Plan Investment Fund	$ 11,358	$ 10,487	$ 10,369	$ 10,442	**$ 10,063**	$ 8,827
Ontario Teachers' Pension Fund	13,822	13,213	12,252	11,535	**11,043**	10,387
Ontario Municipal Employees Retirement Fund (OMERS)	697	666	622	569	**502**	266
Colleges of Applied Arts and Technology Pension Plan	91	89	86	81	**73**	43
Ryerson Retirement Pension Plan	9	8	8	7	**6**	5
Canada Mortgage and Housing Corporation	1,246	1,208	1,181	1,147	**1,100**	1,066
Public Service Pension Fund	3,681	3,604	3,535	3,446	**3,331**	3,200
Ontario Public Service Employees' Union Pension Fund (OPSEU)	1,749	1,712	1,679	1,637	**1,582**	1,520
	$ 32,653	$ 30,987	$ 29,732	$ 28,864	**$ 27,700**	$ 25,314
Publicly Held Debt						
Debentures and Bonds [3]	$ 68,199	$ 72,464	$ 72,549	$ 73,279	**$ 76,502**	$ 77,012
Treasury Bills	675	950	3,002	2,680	**2,118**	2,118
U.S. Commercial Paper [3]	—	272	396	523	**809**	809
Other	455	460	458	447	**447**	444
	$ 69,329	$ 74,146	$ 76,405	$ 76,929	**$ 79,876**	$ 80,383
Total Debt Issued for Provincial Purposes	$101,982	$105,133	$106,137	$ 105,793	**$107,576**	$105,697
Debt Issued for Investment in Electricity Sector [4]	—	—	$ 8,885	$ 8,885	**$ 8,885**	$ 8,885
Deposits with Province of Ontario Savings Office	$ 2,245	$ 2,517	$ 2,812	$ 2,482	**$ 2,444**	$ 2,500
Other Liabilities [5]	$ 21,995	$ 19,237	$ 19,403	$ 16,798	**$ 15,600**	$ 15,825
Total Liabilities:	$126,222	$126,887	$137,237	$ 133,958	**$134,505**	$132,907
Less: Financial Assets [6]	$ (13,487)	$ (12,150)	$ (23,522)	$ (23,324)	**$ (23,998)**	$ (22,411)
Net Provincial Debt	$112,735	$114,737	$113,715 [6]	$ 110,634 [7]	**$110,507**	$110,496

Source: Ontario Ministry of Finance.

(1) The definition of Net Provincial Debt for 2002-03 has been adjusted to include the Net Investment in Capital Assets. For all years, Net Provincial Debt represents total Liabilities less Financial Assets. Prepared on the basis of modified accrual and consolidation accounting.

(2) Includes debt issued by Government Organizations.

(3) All balances are expressed in Canadian dollars. The balances above reflect the effect of related derivative contracts entered into by the Province.

(4) Debt issued for investment in Electricity Sector comprises notes payable to Ontario Electricity Financial Corporation as a result of a debt for equity swap between the Province and its two wholly owned subsidiaries, Ontario Power Generation Inc. and Hydro One Inc.

(5) Other Liabilities includes Accounts Payable, Accrued Liabilities, and Pensions.

(6) Financial Assets comprise Cash and Temporary Investments, Accounts Receivable and Investment in Government Enterprises (including $8,885 million of investment in Electricity Sector).

(7) For more information on Net Provincial Debt (Accumulated Deficit), please see 2000-01 Public Accounts of Ontario, Statement of Financial Position.

Credit Ratings

A credit rating is a current assessment of the creditworthiness of a borrower with respect to a specified obligation. It indicates the capacity and willingness of a borrower to pay interest and principal in a timely manner.

Long-term Ratings

Long-term ratings are assigned a letter grade ranging from investment grade. to speculative grade. to highly speculative or default. Ratings within each category may include a "+" or "-" (or a high or low) to indicate the relative strength of the rating within that category. The current long-term ratings of the Province of Ontario are as follows.

- **Standard & Poor's Corporation (New York)** **AA**
- **Moody's Investors Service (New York)** **Aa2**
- **Dominion Bond Rating Service (Toronto)** **AA**

Short-term Ratings

Short-term ratings are for debt maturities of less than one year. Ratings are graded into several categories. ranging from the highest-quality obligations to default. The current short-term ratings of the Province of Ontario are as follows:

- **Standard & Poor's Corporation (New York)** **A-1+**
- **Moody's Investors Service (New York)** **P-1**
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The Luxembourg Stock Exchange

The London Stock Exchange

The Stock Exchange of Hong Kong

The Stock Exchange of Singapore

The Frankfurt Stock Exchange

The Paris Bourse

The Stock Exchange of Zurich

The Amsterdam Stock Exchange

Additional Sources of Information

Internet: www.ofina.on.ca

Provides information on Ontario's debt, debt issues and retail products and contains publications from the Ontario Financing Authority and Ontario Ministry of Finance.

Publications

- **Ontario Budget**
  Paper D, Ontario's Financing Plan, provides a discussion of the Province's borrowing and debt management activities for the fiscal year ended and reviews the outlook for the fiscal year ahead.

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Contact Addresses and Numbers

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